

H

OUSING MARKET

OUTLOOK

Québec

Housing starts will stay high

Canada Mortgage and Housing Corporation

www.cmhc.ca

Despite an anticipated slight decline, residential construction will stay very active in 2005 in the Québec census metropolitan area (CMA). In fact, 5,800 housing starts are forecast, for a decrease of 6 per cent in relation to the peak reached in 2004. The slowdown will be somewhat more marked next year, as starts should fall by 17 per cent to 4,800 units. For the two years, the expected number of new dwellings will stay above the anticipated household formation levels (4,400 in 2005 and 4,000 in 2006)¹. This difference remains possible because the existing home market has still not attained a balance, for either properties for sale or dwellings for rent. But the gap is tending to narrow.

In the case of freehold housing (single-detached, semi-detached and row, and duplex homes), construction will continue to sail near the peaks in 2005, as 3,200 starts are expected, or almost as many as the total for 2004 (3,311 units). The smaller price increase for new homes than for existing homes has made the former more competitive in recent years. In fact, since 2000, the median price of existing homes has climbed by 48 per cent, compared to an increase of 23 per cent in the Statistics Canada New Housing Price Index. In addition, the resale market is still suffering from a lack of properties for sale, which is inciting some buyers to turn to new homes. However, this advantage will tend to diminish in 2006, as existing

SPRING-SUMMER 2005

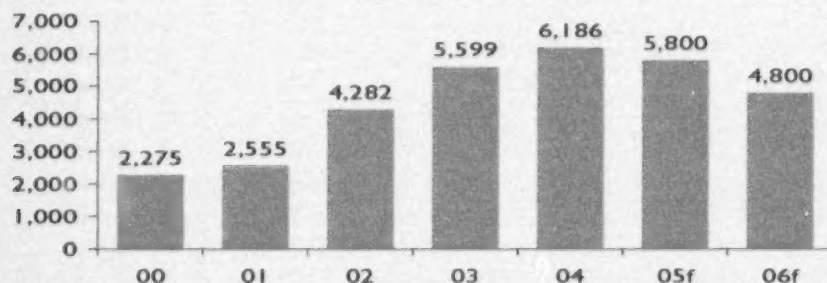
IN THIS ISSUE

- 1 Housing starts will stay high
- 2 Resale market remains active but price increase slows down
- 3 Vacancy rate slowly going back up
- 3 Mortgage rates remain low and employment growth resumes
- 4 New outlook on changes in existing home prices

5 FORECAST SUMMARY

Residential Construction: Smooth Shift

Total Housing Starts – Québec CMA



Source: CMHC
f. forecasts

¹ Household formation in the Québec CMA, forecast by the Institut de la statistique du Québec (ISQ).

property inventories will be replenished and existing home price increases will align themselves with new home price hikes. It is expected that freehold housing starts will reach 3,000 units in 2006.

For condominium construction, the outlook also remains very good for 2005. In all, construction should get under way on 1,100 units this year, for a decrease of 8 per cent from the peak of 1,200 starts recorded in 2004. Such properties target diverse clients, as they attract both households with a limited budget, who seek the more affordable condominiums, and single or older people, who want to spend less energy on maintaining their home and enjoy better security.

Resale market remains active but price increase slows down

In the Québec area, MLS® sales reached a peak in 2002 (over 7,000 transactions). However, resale activity was down in 2003 and 2004 (6,292 and 6,257 transactions, respectively). The main reason for this downturn was the lack of properties for sale, especially affordable ones. An increase in sales completed without the help of a real estate agent was also noted. In fact, when the market is very active, more homeowners attempt to sell their property themselves to avoid having to pay the agent's commission. For the past few months, though, the winds of change have been felt on the resale market. With the new rise in inventories of properties for sale, some buyers who had postponed their purchases are now coming back to the market. As well, this rapid growth in inventories tends to lengthen the listing periods and lower the price hikes. Buyers are much more patient this year than in the last two or three years. They visit more homes and do

Even with all these amenities, though, condominium construction still presents more pronounced cycles than freehold home building because, when the units are started, a significant share of them have not yet been sold. This results in a lag between the time when units are started and the moment when it becomes apparent that demand is waning and inventories are growing. And, for the last few months, inventories have been on the rise, for both new units that are completed and unoccupied or still under construction, as well as existing units for sale. In fact, in March 2005, there were 222 completed and unoccupied condominiums, and 806 units under construction. This is the largest supply since 1995, and these units are sufficient to meet demand

for 12 months, which corresponds to the average duration of supply for the last 15 years. While this level cannot yet be qualified as a surplus, the fact remains that certain sectors should be closely watched. This is the case for the Sainte-Foy sector, where the duration of supply has exceeded 20 months since the middle of 2004. On the existing home market, there were 730 condominiums for sale in the Québec CMA in the first quarter of 2005, or 52 per cent more than during the same quarter in 2004.

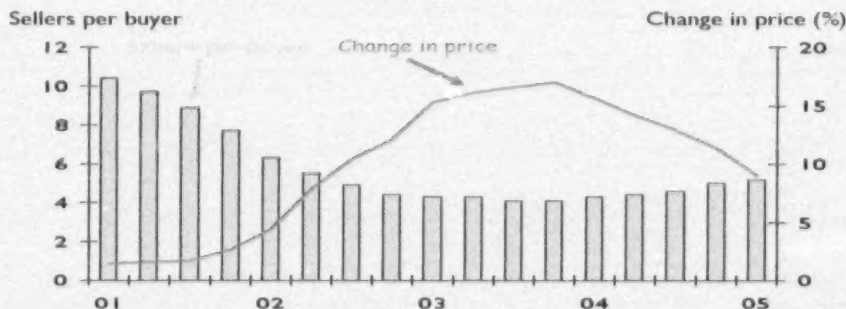
This new rise in inventories on the new and existing home markets will likely slow down construction in 2006, as 700 new units are forecast, for a decrease of 36 per cent.

not jump at the first opportunity. In this context, it can be expected that more homeowners will decide to call on an agent to sell their home. Thanks to these factors and a continued favourable job market, MLS® sales could rise slightly in 2005 and 2006 (to 6,400 and 6,450 units, respectively). These increases will be modest, however, as the strong price hikes in recent years have made properties less affordable. As well, any eventual rise in mortgage rates will add to the negative impact of the price increases.

In the case of home prices, the hikes above 10 per cent that we saw in the last three years are now a thing of the past. In fact, with the increase in inventories, the number of sellers per buyer has now started rising again, as it went from a low of 4.1 in the first quarter of 2004 to 5.2 in the first quarter of 2005. From an overheating market (less than 5 sellers per buyer) between 2002 and 2004, we will now shift to a seller's market (between 5 and 8 sellers per buyer) in 2005 and for a good part of 2006. A balanced

Resale Market: Price Increases Running out of Steam

Sellers per Buyer and Change in MLS® Price – Québec CMA



Source: CIQ (CMHC compilation)

market (between 8 and 10 sellers per buyer) could be achieved in late 2006 or early 2007. As a result, the rise in the median price will slow down from 11.4 per cent in 2004 to 6.5 per cent in 2005 and then to 3.3 per cent in

2006. The condominium segment will no doubt be the first to become balanced, as the supply is rising rapidly on this market, and the price rises should therefore be smaller. The single-detached and semi-detached

and row home markets should then follow suit. The return to a balanced market for this last housing type, and the resulting price changes, generally take place with a lag (see note 3 in the box on page 4).

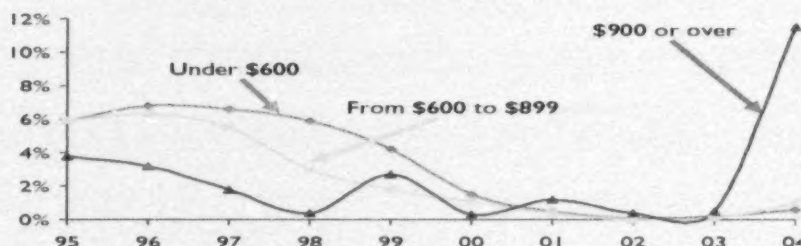
Vacancy rate slowly going back up

The housing shortage prevailing in the Québec area has eased in recent years, as the vacancy rate went up from 0.3 per cent in 2002 to 1.1 per cent in 2004. However, the rental market remains tight, and many tenants are still experiencing difficulty in finding an apartment that meets their needs, especially among the most affordable units. In fact, only 0.6 per cent of all two-bedroom apartments renting for under \$600 per months were available in 2004. This proportion rose to 1.0 per cent for units with rents between \$600 and \$899 and shot up to 11.5 per cent when the rental rate was \$900 or over. This explosion in the vacancy rate for expensive units resulted from the massive arrival of more than 700 apartments of this type in the Sainte-Foy sector and the strong competition from home buying among potential clients for luxury units, especially in a context of low interest rates.

This saturation in the upscale segment will somewhat hold back rental housing construction in 2005.

High Vacancy Rate for Luxury Units

Vacancy Rate (%) by Rent Range – Québec CMA
Two-Bedroom Apartments



Source: CMHC

Activity will still remain vigorous thanks to the start-up of a greater number of apartments for seniors. It is therefore expected that construction will get under way on 1,500 rental housing units in 2005, for a decrease of 10 per cent from 2004. The decline will be more significant in 2006 as, in addition to the luxury segment of the traditional rental market, the retirement apartment market will also be saturated. As well, most of the social housing units resulting from the different government programs will have already been developed, which will put additional downward pressure

on the level of activity. Starts should therefore attain 1,100 units in 2006, down by 27 per cent.

The anticipated slowdown in demand, in a context where the growth in households is weaker, along with a continued large supply of new units, will keep the vacancy rate on the rise in 2005 and 2006. This rise will be moderate, though, and the vacancy rate could reach 1.5 per cent in 2005 and 1.8 per cent in 2006. As for the average rent, it should go up by 3 per cent per year, which will still be above inflation (target rate of 2 per cent).

Mortgage rates remain low and employment growth resumes

The appreciation of the Canadian dollar against the U.S. dollar held back economic expansion in the country and, by the same token, delayed the key policy interest rate rise initiated by the Bank of Canada in 2004. This situation kept mortgage rates at historically low levels. And, there is every indication that this situation will

last for several more quarters, as the anticipated rise in the rates will take place gradually and should only begin during the second half of the year. Our latest forecasts call for an increase at the end of 2005 that should continue throughout 2006. The average rate for a one-year term will therefore be 5.2 per cent at the end of this year and 5.7 per cent by the fourth quarter of 2006. The longer-term rate (five-year term), for its part, will attain levels of 6.5 per cent and 6.8 per

cent, respectively, at the end of the fourth quarters of 2005 and 2006.

As for the job market, after posting record growth in 2001 and 2002, it took a breather in 2003, with a small loss of jobs. This calm period was short-lived, however, as this market undeniably picked up again right away in 2004. For 2005 and 2006, respective gains of 5,000 jobs (+1.5 per cent) and 4,000 jobs (+1.1 per cent) are anticipated.

A favourable job market and a small gradual rise in mortgage rates will

therefore allow the housing market to make a smooth landing and the resale

and rental markets to progressively return toward a better balance.

New outlook on changes in existing home prices

There are several advantages to using the average price of properties sold through the S.I.A.[®]/MLS[®] to measure the increase in the price of existing homes: fast access, reduced manipulation, detailed data and broad market coverage. The major disadvantage lies in the fact that the changes in the intrinsic value of homes are blended in with the changes in the sales mix¹, such that it is impossible to determine the shares of each of these types of changes.

At CMHC, we have developed a methodology² that removes most of the sales mix effect and provides a much closer estimate of the actual increase in the value of homes. The following therefore presents a new outlook on the changes in the "cleaned-up" median price of existing homes in the Québec CMA over the last ten years.

Between 1994 and 2004, the median price of single-family homes in the Québec CMA went up from \$82,000 to \$127,500, which represents an increase of 55 per cent or

\$45,500. During this period, there were three years in which the value of properties went down: 1995, 1996 and 1998. The decreases were small, never exceeding 1.8 per cent. Conversely, it was during the period from 2002 to 2004 that the value went up the most rapidly, with annual increases surpassing 10 per cent.

Semi-detached and row homes, while less numerous and slightly contra-cyclical³, managed to do very well. In fact, over the ten-year period, the increase in their value was similar to the rise in the value of single-detached houses. As a result, just like in 1994, the median price of semi-detached and row homes represented 86 per cent of the median price of single-detached houses in 2004.

Small homes (less than 800 square feet) also served their owners well. Over ten years, their value went up by 62 per cent, compared to 56 per cent for homes of 800 to 1,100 square feet, and 55 per cent for houses of more than 1,100 square feet. Somewhat like

on the stock market, holdings with a high value at the outset often present a smaller growth potential.

The age of a property also has an impact on the increase in its value. Newer homes, aged from 1 to 10 years, posted the largest increase in value between 1994 and 2004, at 65 per cent or \$54,500, followed by homes aged from 11 to 25 years, for which the gain was 61 per cent or \$49,000. The value of houses aged 26 years or older went up less significantly, as the rise was limited to 49 per cent or \$41,000.

Lastly, it was zone 5 (Val Bélair, Saint-Émile) that showed the greatest increase in value, at 64 per cent in 10 years, followed by zone 8 (south shore near the bridges), at 63 per cent. In monetary terms, however, owners in zone 2 (Haute-Ville) were the ones who benefited from the largest equity gain, at \$74,500. Finally, it was zone 1 (Basse-Ville, Vanier) that posted the smallest gain, both in percentage and absolute terms, at 40 per cent or \$31,500.

Changes in Values by Zone

Zone	Price - 1994 (\$)	Price - 2004 (\$)	Chg. (%)	Chg. (\$)
1	79,000	110,500	40	31,500
2	158,000	232,500	47	74,500
3	80,000	126,000	58	46,000
4	107,950	153,000	42	45,050
5	73,000	120,000	64	47,000
6	82,000	124,900	52	42,900
7	82,000	126,500	54	44,500
8	78,000	127,000	63	49,000
9	79,000	121,000	53	42,000
CMA	82,000	127,500	55	45,500

Description of the Québec metropolitan area market zones:

Zone 1: Basse-Ville de Québec, Vanier

Zone 2: Haute-Ville de Québec

Zone 3: Ancienne-Lorette, Neufchâtel, Duberger, Les Saules, Lebourgneuf

Zone 4: Sainte-Foy, Sillery, Cap-Rouge, Saint-Augustin

Zone 5: Val-Bélair, Saint-Émile, Loretteville, Lac Saint-Charles, Lac Delage, Valcartier, Shannon, Lac Saint-Joseph, Sainte-Catherine-de-la-Jacques-Cartier, Fossambault

Zone 6: Grand Charlesbourg, Lac Beauport, Stoneham-Tewkesbury

Zone 7: Grand Beauport, Sainte-Brigitte-de-Laval, Boischâtel, L'Ange-Gardien, Château-Richer, Île d'Orléans

Zone 8: Charny, Saint-Romuald, Saint-Jean-Chrysostôme, Saint-Nicolas, Saint-Rédempteur, Breilleyville, Saint-Lambert, Saint-Étienne

Zone 9: Lévis, Pintendre, Saint-Joseph-de-Lévy, Beaumont

¹ For example, a greater proportion of sales of upper-range properties from one year to the next will inflate the average price.

² This methodology comprises several steps to clean up the original data, including one step that uses the statistical method called hierarchical classification. Once the clean-up is complete, we calculate the median value. To find out more about this method, contact us.

³ Since demand for single-detached houses is stronger than for semi-detached and row homes during the expansion phase of the real estate cycle, the price of the latter tends to grow more slowly. However, given their more modest price, semi-detached and row homes tend to see their demand and price rise more significantly during the contraction phase of the real estate cycle.

Forecast Summary

Québec Census Metropolitan Area

Spring-Summer 2005

	2003	2004	2005f	2006f	2004/2005	2005/2006
RESALE MARKET ¹						
MLS® sales						
Total	6,292	6,257	6,400	6,450	2.3%	0.8%
Single-detached	3,977	3,962	4,040	4,050	2.0%	0.2%
Semi-detached and row	943	887	900	925	1.5%	2.8%
Condominium	1,056	1,123	1,160	1,175	3.3%	1.3%
Duplex	316	285	300	300	5.3%	0.0%
Active MLS® listings						
Total (annual average)	2,170	2,609	3,400	4,100	30%	21%
Median MLS® price (\$)						
Total	114,271	127,281	135,500	140,000	6.5%	3.3%
Single-detached	122,499	134,850	143,600	148,500	6.5%	3.4%
Semi-detached and row	95,814	112,534	122,000	127,000	8.4%	4.1%
Condominium	98,522	108,041	111,800	114,000	3.5%	2.0%
NEW HOME MARKET						
Starts						
Total	5,599	6,186	5,800	4,800	-6.2%	-17.2%
Freehold	3,167	3,311	3,200	3,000	-3.4%	-6.3%
Condominium	1,070	1,200	1,100	700	-9.3%	-36.4%
Rental	1,362	1,675	1,500	1,100	-10.4%	-26.7%
New Housing Price Index						
1997 = 100	121.9	129.3	134.5	138.5	4.0%	3.0%
RENTAL MARKET (%)						
Vacancy rate (October)	0.5	1.1	1.5	1.8	--	--
Change in rents (2-bedroom)	3.4	4.5	3.0	3.0	--	--
ECONOMIC OVERVIEW						
Mortgage rate - 1-year (%)	4.8	4.6	5.0	5.6	--	--
Mortgage rate - 5-year (%)	6.4	6.2	6.3	6.7	--	--
Employment level	360.0	364.7	370.0	374.0	1.5%	1.1%
Unemployment rate (%)	7.0	5.7	6.5	6.5	--	--

¹ The publication of MLS® data is made possible thanks to the collaboration of the Chambre immobilière de Québec (CIQ).

f: CMHC forecasts

Sources: CMHC, CIQ and Statistics Canada

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